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APR 16

In the Supreme Court

OF THE

United States

October Term, 1931

GEORGE P. PORTER, State Auditor and ex officio Investment Commissioner of the State of Montana,

Appellant,

vs.

INVESTORS SYNDICATE, a corporation,

Appellee.

BRIEF OF APPELLANT

Appeal from the District Court of the United States, in and for the District of Montana.

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Filed, April....., 1932.

.....Clerk

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Appeal from the District Court of the United States, in and for the District of Montana.

APPELLANT'S BRIEF

This is an appeal under Section 266 of the Judicial Code, as amended, (28 U. S. C. 380) from an order of the District Court of the United States, in and for the District of Montana, enjoining the enforcement of an order of the State Auditor and ex officio Investment Commissioner of Montana, which order required all "Investment Companies" to provide in their contracts that

the "Purchaser of its Investment Certificates" might withdraw all amounts paid in by him, at his option at any time after the end of a year, less only a forfeiture of three and one-half (3½%) per cent of the face value of the certificate, that is $35.00 on an investment ceritficate for $1,000.00.

OPINION

The opinions of the three judge court are set forth in 52 F. (2d) 189.

STATEMENT OF THE CASE

Plaintiff is a Minnesota corporation engaged in the business of selling Investment Certificates, which may be described as certificates which the purchaser pays for, in installments and at the end of a given period, e. g., ten years, on the surrender of his certificate receives the face value of the certificate, e. g., $1,000.00.

The certificate is supposed to return its owner five and one-half (5½%) per cent interest compounded on all installments paid at maturity. The form of certificate in use by plaintiff (R. p. 13) causes the purchaser to forfeit all payments made during the first eighteen months in case he defaults in payments. After eighteen months, and after payment of $148.00 on a $1,000.00 certificate, ($111.00 if paid in installments) (all certificates will hereafter be treated, for convenience, as $1,000.00 certificates), he may receive on surrender of his certificate $42.00,

forfeiting $106.00, or $69.00. After four years and payment of $370.00 (or $296.00) he may close the books and draw $254.00, forfeiting $116.00 (or $42.00) and his interest. Not in any event until he has paid in for five years can be get back his payments in full.

The certificate is drawn on the basis of payment of five and one-half (5½%) per cent interest.

Plaintiff was first licensed by the Investment Commission of Montana in 1930 (R. p. 2) and was then selling a certificate substantially though not exactly the same as at the time of the order hereinafter referred to—has over twenty-two agents selling its certificates—and sold over $2,141,200 face value of such certificates in Montana in 1930. It sells the same form of certificate in thirty-five other states and provinces of Canada (R. p. 7).

The defendant is the Investment Commissioner of Montana. Section 4043, Revised Codes of Montana, provides:

> "* * * The Investment Commissioner shall have general supervision and control, as provided by this act, over any and all investment companies and stock brokers, domestic or foreign, licensed under this act."

Defendant is given the power to revoke permits of investment companies in Montana (Section 4045, R. C. M., 1921) when such a company is

"conducting its business in an unsafe, inequitable or unauthorized manner."

On May 7, 1931, the Investment Commissioner served notice on defendant with a number of others to attend a hearing relative to the promulgation of the rule in question in this case.

Plaintiff appeared by his vice-president and Mr. M. S. Gunn of counsel and voiced plaintiff's objection to the rule as appears by the following quotation taken from the Commissioner's statement accompanying the Order and set forth as an exhibit in the Answer (Tr. p. 19):

BEFORE GEO. P. PORTER, STATE AUDITOR AND EX OFFICIO INVESTMENT COMMISSIONER

Hearings held May 23 and June 1, 1931, at the State Capitol Building, Helena, Montana. The following appearances were made:

Investors Syndicate and Installment Securities Agency, Incorporated, H. W. Berg, Vice-President and M. S. Gunn, Counsel.

Universal Bond and Mortgage Company, Paul Hudtloff, Vice-President, H. J. Fennimore, Director and Frank Venable, Montana Manager.

International Guaranty Thrift Corporation, F. M. Zimmers, President.

Great Western Bond & Mortgage Corporation—by written record.

Decker Mortgage Company—no appearances.

National Thrift Corporation of America—no appearances.

National Bond Corporation, R. M. Tone, President.

National Mortgage Bond Corporation of Montana—no appearances.

United Bond and Finance Corporation, Guy M. Miller, State Manager and Earle Genzberger, Counsel.

The corporations cited to appear in this action were all engaged in selling in Montana installment certificates, bonds and other securities creating a debtor-creditor relationship on the installment plan. The general procedure is to sell certificates on the basis of One Thousand Dollar debenture at maturity, at the rate of approximately $6.25 per month, with the security maturing at periods generally ranging from ten to eleven years. In computing the maturity value the interest rate offered varies from 5½% to 7%, which is included ni the aggregate in determining the maturity value of the security. The character of the security ranges from promissory notes to bonds and in certain cases financial institutions act as trustees, but in others it has been the policy for the company to be the guarantor. These contracts carry a provision that no withdrawals will be permissible prior to periods ranging from 18 months to three years. Furthermore, the provisions of the contract provide that

in the event a subscriber desires to withdraw and terminate his contract that the withdrawal value of said certificate shall be the amount paid in, less penalty ranging from 3½% to 8% of the matured value of the security. The penalty is ordinarily called a loading charge and the companies attempt to justify the same on the grounds that it is one of their methods of procuring funds for selling costs and general operation.

As an example of an aggravated case the Commissioner has a complaint from a subscriber who has paid $260.00 on a $2500.00 contract and 26 payments of $10.00 each and upon his application to withdraw the company offered to return $60.15.

A portion of the Investment Companies in this action were operating in Montana prior to the enactment of the present Investment Act while others have filed with the Commissioner since that time.

The present period of depression has largely changed conditions and wage earners who were the principal subscribers for installment securities find themselves without positions and unable to continue payments on their contracts. The majority of the complainants seem to be of the opinion that they can withdraw their money and when exorbitant penalties are imposed, the resultant effect is apparent.

This hearing resolves itself into two issues—

FIRST, that installment companies shall make settlement with their subscribers at any time after the contract has been in effect one year, upon service of proper notice.

SECOND, that the maximum withdrawal penalty allowed shall not exceed 3½% or $35.00 per thousand, of the face or matured value of the security.

Prior to the hearing the Commissioner served the following notice on each of the Investment Companies included herein:

> "Complaints having been made to the Investment Commissioner that the penalties for withdrawals fixed by investment companies operating in the State of Montana are excessive, unfair, unjust, inequitable and oppressive, to its contributors as provided in Section 4036 of the Revised Codes of Montana, 1921,
>
> THEREFORE, you, and each of you, are hereby notified that this Commission will at 2:00 o'clock P. M. on the twenty-third day of May, 1931, at the office of the Commissioner, at the State Capitol, at Helena, Montana, conduct a hearing relative to promulgating the following rule:
>
> 'In the interests of the investing public, any investment company operating in the State of Montana shall not issue, sell or distribute, any bonds, certificates of indebtedness, collateral trust certificates or any other device whatsoever, that might be deemed a security creating a debtor-creditor relationship, which has a withdrawal privilege, before maturity, that does not provide for withdrawal of installments paid thereon due any time after the first year, if the owner or holder shall have given ninety (90) days notice in writing of his intention to make

such withdrawal and such owner or holder shall be entitled to receive the total amount of all installments paid in, less only a withdrawal penalty not exceeding three and one-half (3½) per cent of the matured or face value of such securities, plus interest compounded annually at the rate at which said securities are guaranteed to mature or represented to pay at maturity; and provided further, that the bond or contract representing such security and the application for the same shall have printed thereon, the amount paid in, the withdrawal or surrender value thereof, and the loan value at the end of each year of its duration.

IT IS FURTHER PROVIDED that none of the above securities as enumerated shall be permitted to be sold in the State of Montana unless there is a withdrawal privilege provided each year beginning with the first year until maturity.'

You and each of you are hereby given an opportunity to appear and present any objections you may have as to the reasonableness of said proposed ruling.

Dated at Helena, Montana, this seventh day of May, 1931.

(Signed) Geo. P. Porter, State Auditor and ex officio Investment Commissioner."

The Commissioner on June 22, 1931, ordered that the rule be adopted to go into effect July 22, 1931.

The Commissioner asserted that he intended to revoke the license of plaintiff to sell its certificates in Montana unless plaintiff complied with the rule, and plaintiff brought a Bill of Complaint in Equity to enjoin the Commissioner from "invoking or purporting to revoke or attempting to revoke plaintiff's permit because of

the failure of plaintiff to comply with said order." (R. p. 9.)

The action was tried before a three judge court on motion for a temporary restraining order. On stipulation after the hearing the case was submitted for final determination (R. p. 31).

Judgment restraining the Commissioner as prayed for was entered and the Commissioner appeals from such final order and decree.

Sawtelle, Circuit Judge, and Pray, District Judge, signed the majority opinion (R. p. 43). Bourquin, District Judge, dissented (R. p. 47).

STATUTES INVOLVED

Statutes involved are as follows: Section 4043 Revised Codes of Montana, 1921:

> "Supervisory control and fees of commissioner. The investment commissioner shall have general supervision and control, as provided by this act, over any and all investment companies and stock-brokers, domestic or foreign, licensed under this act, and all such investment companies or stock-brokers shall be subject to examination by the investment commissioner, or his duly authorized agents or deputies, at any time the investment commissioner may deem it advisable, and in the same manner as is now provided for the examination of state banks. The rights, powers, and privileges of the investment commissioner in connection with such examinations shall be the same as is now provided with reference to the examination of state banks. Such investment company or stock-broker shall pay a fee for each examination made by said investment commissioner, or his deputies or agents, of not to exceed ten dollars for each day or fraction

thereof, plus the actual traveling and hotel expenses of said commissioner, or his agent or deputy, that he is absent from the capitol building for the purpose of making such examination, and the failure or refusal of any investment company or stock-broker to pay such fees upon the demand of the investment commissioner, or his deputy or agent, while making such examination, shall work a forfeiture of his or its right to do business in this state."

Section 4045, Revised Codes of Montana, 1921:

"Revocation of permits and appointment of receiver. Whenever it shall appear to the investment commissioner that the assets of any investment company doing business in this state are impaired to the extent that such assets do not equal its liabilities, or that it is conducting its business in an unsafe, inequitable, or unauthorized manner, or is jeopardizing the interests of its stockholders or the investors in stocks, bonds, or other securities by it offered for sale, or whenever any investment company shall refuse to file any papers, statements, or documents required under this act, or shall refuse to permit an examination by said investment commissioner, or his deputies or agents, as provided in this act, without giving satisfactory reasons therefor, said investment commissioner shall at once cancel its permit, and if he shall deem advisable, shall communicate such facts to the attorney-general, who shall thereupon at once make an investigation, and if the facts as presented to him by the investment commissioner are substantiated, he shall thereupon apply to a court of competent jurisdiction for the appointment of a receiver to take charge of and conclude the business and affairs of such investment company, and if such fact or facts be made to appear, it shall be sufficient evidence to authorize the appointment of a receiver and the making of such orders and

decrees in such cases as equity may require."

Section 4036, Revised Codes of Montana, 1921, provides as follows:

> "It shall be the duty of the investment commsisioner to examine the statements and documents so filed, and if said investment commissioner shall deem it advisable, he shall make or have made a detailed examination, audit or investigation of such investment company's affairs; providing, that such investment company may at its option, in writing, refuse to have such investigation made, in which event said investment commissioner shall reject its application. If he finds that such investment company is solvent, that its articles of incorporation or association, its constitution and by-laws, its proposed plan of business, and proposed contracts contain and provide for a fair, just and equitable plan for the transaction of business, and in his judgment promises a fair return on the stocks, bonds, or other securities by it offered for sale, the investment commission shall issue to such investment company a statement, entitling it to sell such securities in the state of Montana, and reciting that such company has complied with the provisions of this act, that detailed information in regard to the company and its securities is on file in the investment commissioner's office, and that such investment company is permitted to do business in this state; and such statement shall also recite in bold type that the investment commissioner in nowise recommends the securities to be offered for sale by such investment company. Such permit, however, shall be subject to revocation at any time by the investment commissioner for cause to him sufficient. But if said investment commissioner finds that such articles of incorporation or association, charter, constitution, and by-laws, plan of business, or proposed contract contain any provision that is unfair, unjust,

inequitable, or oppressive to any class of contributors, or if he decides from his investigation or examination of its affairs that said investment company is not solvent, or does not intend to do a fair and honest business, or in his judgment does not promise a fair return on the stocks, bonds, or other securities by it offered for sale, then he shall not grant such company a permit as herein provided, and shall notify said company in writing of his decision."

Section 4038 as amended by Chapter 194, Montana Session Laws of 1931:

"Any interested person, who has appeared, co-partnership, association or corporation being dissatisfied with any finding, findings or decision of the commissioner made in accordance with the provisions of this act, may within thirty days from the making thereof, commence an action in any court of competent jurisdiction against said commissioner as defendant, to vacate and set aside said finding, findings or decision, on the ground that the said findings or decision are unjust or unreasonable. The rules of pleading and procedure in such action shall be the same as are provided by law for the trial of equitable actions in the district courts of this state and on the hearing the judge of said court may set aside, modify or confirm said findings or decision as the evidence and the rules or equity may require. Appeals may be taken from the decision of the district court to the supreme court by either party in the same manner as is provided by law in other civil actions. Pending any such action, the said findings or decision of said commissioner shall be prima facie evidence that they are just and reasonable and that the facts found are true, and pending any such action the said findings or decision of the commissioner shall remain in full force and effect. If no action be brought to set aside said findings or decision within

thirty days, the same shall become final and binding.

"Provided, however, that the original application with reference to which an appeal is herein provided for shall not be heard by the investment commissioner until notice of hearing on the same has been published in some newspaper published at the capital city daily, in at least seven issues of such paper, and provided further, that upon such hearing on the original application, any person, co-partnership, association or corporation interested in or opposed to said application may appear."

For possible questions arising we have appended a pamphlet setting out the entire Blue Sky Laws of Montana.

SPECIFICATIONS OF ERRORS

Appellant specifies the following errors which it intends to urge:

I.

The bill of complaint does not state facts sufficient to constitute a valid cause of action in equity or at all (argued last).

II.

The United States District Court for the District of Montana erred in holding that code sections 4043, 4036 and 4045, Revised Codes of Montana, 1921, and Chapter 194 of the Session Laws of 1931 (Blue Sky Laws) are void as violative of the due process clause of the Fourteenth Amendment to the Federal Constitution in that the law, itself, makes no provision for notice or opportunity for hearing by an investment com-

pany whose license the investment commissioner may be threatening to revoke.

III.

The United States District Court for the District of Montana erred in holding that the guaranty of the due process clause of the Fourteenth Amendment to the Federal Constitution is challenged when an order is made by the commissioner, based upon the above mentioned Blue Sky Laws, and with or without actual notice revoking a license or permit, such order to be in effect pending the test of its validity by the court.

IV.

The United States District Court for the District of Montana erred in holding that the Montana Blue Sky statutes and threatened procedure of the defendant are violative of the due process clause of the Fourteenth Amendment to the Federal Constitution in that no rule or standard is provided in such statutes to determine when sufficient cause for revocation of a license exists or when a given business is being conducted in an inequitable manner.

V.

The United States District Court for the District of Montana erred in holding that the Montana Blue Sky statutes violate Section 1 of Article V of the Constitution of Montana in that they require the defendant to exercise legislative power and to, himself, set up a legislative stand-

ard when he undertakes to say whether a certain business is being conducted in an inequitable manner.

VI.

The United States District Court for the District of Montana erred in holding that the Montana Blue Sky laws are violative of the Fourteenth Amendment to the Federal Constitution (privileges and immunities clause) in that the police powers which may be exercised by the legislature of a state do not permit them to regulate the sale of securities or the making of contracts, such regulations to rest in the judgment of the investment commissioner of the state as to whether or not such sales or contracts are equitable (IV., V., and VI. argued together).

VII.

The United States District Court for the District of Montana erred in enjoining the defendant from enforcing his order as against the plaintiff, such order being that it conform to rules promulgated by the commissioner with reference to forfeiture clause and investment contract.

SUMMARY OF ARGUMENT

1.

Where the statute provides for an appeal to the courts as to the reasonableness of the action of an executive officer "due process" does not require the statute to provide for notice and hearing before such executive officer before he

takes action, such as the revocation of a permit.

2.

If such notice is necessary it will be implied.

3.

"Due process" does not require that the legislature set up a definite standard of equity to apply to all cases. If the conditions are within the power of the legislature to impose they may, and can only be, ascertained by the commissioner in such case as this.

4.

Imposition on credulity and ignorance may be prevented as may fraud by active misrepresentation, under the police powers of the state.

5.

The plan of business of the plaintiff as shown in the certificate set up in its Bill of Complaint in requiring the forfeiture shown on the certificate is inequitable and its Bill of Complaint does not state a cause of action in equity.

ARGUMENT

The majority opinion, R. page 33, determined that the Montana statute challenged the due process of law clause of the Fourteenth Amendment:

I.

In that the statute failed to provide for notice to the plaintiff of the promulgation of the order before the revocation of his certificate on his failure to comply with the order.

II.

In that the statute provided no standard by which the commissioner could determine what was "inequitable" in the conduct of a given business.

These holdings have been specified as error (R. p. 48).

DUE PROCESS OF LAW

Montana Revised Codes, Section 4036, in force before plaintiff came into the state authorizes the revocation of a certificate "at any time by the commissioner for cause to him sufficient."

By the provisions of code Section 4045 the commissioner is authorized to cancel a permit "whenever it shall appear to the investment commissioner that it is conducting its business in an unsafe, inequitable or unauthorized manner."

There is no provision in those statutes for notice to the investment company, but Section 4038 as amended by Chapter 194 of the 1931 Session Laws provides for an appeal to the District Court (a court of general jurisdiction), and likewise from the District Court to the Supreme Court from "any finding, findings or decision of the commissioner made in accordance with the provisions of this act and the Blue Sky Law."

The majority opinion reads (R. p. 37):

> "The principal contentions of plaintiff are that Section 4036 Revised Codes of Montana, 1921, which authorizes the revocation of a permit 'at any time by the investment com-

missioner for cause to him sufficient,' and the provision of Section 4045, which authorizes the cancellation of a permit whenever it appears to the investment commissioner that the permittee is conducting its business in an inequitable manner, are in violation of the due process of law clause of the 14th amendment to the Constitution of the United States for failure to provide for notice and opportunity for hearing; and for the further reason that no rule or standard is fixed for determining what is a sufficient cause or when the business is being conducted in an inequitable manner.

"Although in this case a hearing was in fact accorded plaintiff, the Blue Sky Law itself, which was relied upon by the investment commissioner, makes no provision for notice or opportunity to be heard. 'If the statute did not provide for a notice in any form, it is not material that as a matter of grace or favor notice may have been given of the proposed assessment. It is not what notice, uncalled for by the statute, the taxpayer may have received in a particular case that is material, but the question is whether any notice is provided for by the statute.' Coe vs. Armour Fertilizer Works, 237 U. S. 413, citing Stewart vs. Palmer, 74 N. Y. 183, 188, 30 A. Rep. 289, involving the validity of a statute assessing the expense of a local improvement upon the land benefited without notice to the owner. According to the weight of authority, although the owner may have been given notice and even a hearing, indicating a desire for fair play on the part of the officer, that is not sufficient to satisfy the constitutional requirement unless the right to such notice and hearing is embodied in the statute. National Automobile Service Corporation vs. Barford, 137 Atl. (Penn.) 601; Garfield vs. U. S. ex rel, Goldsbay, 211 U. S. 249 (not in point); C. M. & St. P. Ry. Co. vs. Board of Railroad Commissioners, 76 Mont. 305; * * *"

The majority opinion (R. p. 39) does hold that the Montana statute above quoted provides for an appeal to the courts of Montana.

It is to be noted that plaintiff appeared at the hearing before the commissioner promulgated the rule in question, filed its protest and took active part in that hearing after notice had been served on plaintiff to appear (R. p. 18).

The question then is: did the provision for appeal to the courts of Montana provide due process of law?

See Section 4038 as amended by Chapter 194, Session Laws of 1931.

> "* * * any interested person who has appeared * * * being dissatisfied with any finding, findings or decision of the commissioner made in accordance with the provisions of this act, may within thirty days from making thereof, commence an action in any court of competent jurisdiction against said commissioner as defendant, to vacate and set aside said finding, findings or decision, on the ground that the said findings or decision are unjust or unreasonable."

In the case of Coe vs. Armour Fertilizer Works, 237 U. S. 413, on which the opinion is founded, an execution had been issued by virtue of a judgment against a corporation but, under the statute, the execution was directed against the property of a stockholder for the amount of his unpaid stock subscription as it showed on the books of the corporation. His property was taken without hearing and he had no appeal to the courts.

It was, of course, held that there was no due process of law.

In Vandalia R. R. v. Public Service Commission, 242 U. S. 255, it was provided by statute that the railroad commission be authorized to investigate the condition and efficiency of headlights in use on locomotives and engines, and to make and enforce against the railroad companies the necessary orders in the installation of such headlights (p. 257). No notice was provided for in the statute. The commission proceeded to make its own investigation. The Court said on page 260:

> "With respect to the question of due process of law, it is unnecessary to determine whether the Fourteenth Amendment requires that state action, legislative in its nature, of the character of the order of the Railroad Commission, shall be preceded by notice and an opportunity for hearing. In the case before us, the Supreme Court of Indiana construed the Act of 1909 as supplemental to the Act of 1905, which, as amended in 1907 (Acts 1907, p. 469, Sec. 6; Burns' Ann. Ind. Stats. 1908, Sec. 5536) gave to any carrier or other party dissatisfied with any order made by the commission a *right to resort to the courts in an action to suspend it or set it aside.* Since the order in question was made after notice and a full hearing, the plaintiff in error had and exercised the right to a judicial review by action at law, we concur in the view of the state court that there has been in this respect no deprivation of property without due process of law."

In Bragg v. Weaver, 251 U. S. 57, by a statute of Virginia it was provided that certain officers engaged in repairing public roads were authorized to take earth for that purpose from adjacent lands, and it then provided for a hearing as to the compensation which the land owners would be entitled to and an appeal to the court.

> "It is true there is no express provision for notice at the inception or during the early stages of the proceedings; and for present purposes it may be assumed that such a requirement is not even implied, although a different view might be admissible. See Paulsen v. Portland, 149 U. S. 30. But the provisions relating to the later stage—the decision by the supervisors—are not silent in respect of notice, but speak in terms easily understood. Clauses 5 and 22 taken together provide that the owner, if dissatisfied with the decision, shall have the right to appeal as in other cases. This presupposes that he will have some knowledge of the decision, and yet neither clause states how the knowledge is to be obtained, or when or how the right of appeal is to be exercised."
>
> "The claim is made that this opportunity comes after the taking, and therefore is too late. But it is settled by the decisions of this court that where adequate provision is made for the certain payment of the compensation without unreasonable delay the taking does not contravene due process of law in the sense of the Fourteenth Amendment merely because it precedes the ascertainment of what compensation is just. Sweet v. Rechel, 159 U. S. 380, 402, 407; Backus v. Fort Street Union Depot Co., 169 U. S. 557, 568; Williams v. Parker, 188 U. S. 491; Crozier v. Krupp, 224 U. S. 290, 306. And See Branson v. Gee, 25 Oregon 462."

THE REQUIREMENT OF NOTICE IS IMPLIED

Paulsen v. Portland, 149 U. S. 30—opinion (by Mr. Justice Brewer) sets forth the following:

> "Thus, in the case of Gilmore v. Hentig, 33 Kansas 156, it was held thus: 'Where a statute authorizes a city to provide for the construction of sewers and drains, and to tax the costs thereof upon the adjacent property owners, but does not require that any notice shall be given to the property owners, held, that such failure to require notice does not render the statute unconstitutional or void, but notice must nevertheless be given, and the city would have a broad discretion with reference to the kind of notice and the manner of giving the same.' See also Cleveland v. Tripp, 13 R. I. 50; Davis v. Lynchburg, 84 Virginia 861; Williams v. Detroit, 2 Michigan 560; Gatch v. Des Moines, 63 Iowa 718; Baltimore & Ohio Railroad v. Pittsburgh, Wheeling &c Railroad, 17 W. Va. 812, 835."

and see Davidson v. New Orleans, 96 U. S. 97 on page 107.

The situation is analogous to the conditions of a burglary—a sheriff on seeing the act may arrest the burglar without warrant or may take his life in certain cases without any more due process than is furnished by the aspects of the case, as they appear to him as a reasonable man. He holds the burglar in jail on indictment or information and deprives him of his liberty pending trial.

See Public Clearing House vs. Coyne, 194 U.

S. 497, on 509. This was a case where the postmaster had refused plaintiff the use of the mails without notice or hearing.

> "Temporary deprivations of liberty or property must often take place through the action of ministerial or executive officers or functionaries, or even of private parties, where it has never been supposed that the common law would afford redress. If the ordinary daily transactions of the departments, which involve an interference with private rights, were required to be submitted to the courts before action was finally taken, the result would entail practically a suspension of some of the most important functions of the government. Even in the recent case of the School of Magnetic Healing v. McAnnulty, 187 U. S. 94, the constitutionality of the law authorizing seizures of this kind by the Postmaster General was assumed, if not actually decided, the only reservation being that the *person injured may apply to the courts for redress in case the Postmaster General has exceeded his authority or his action is palpably wrong.*" (Italics ours.)
>
> "The procedure provided in Section 280 (a) (1) satisfies the requirements of due process because two alternative methods of eventual judicial review are available to the transferee; (a) he may contest his liability by bringing an action, either against the United States or the Collector, to recover the amount paid; or (b) he may avail himself of the provisions for immediate redetermination of the liability by the Board of Tax Appeals, and if dissatisfied, may have a further review by the Circuit Court of Appeals and possibly by this Court on certiorari. Page 597"—Phillips et al., Executors, v. Commissioner of Internal Revenue, 283 U. S. 581, headnote 4.

In support of the majority opinion the Court

cites Garfield vs. U. S. ex rel. Goldsbay, 211 U. S. 249. This case is not in point. The Garfield case was a case where mandamus was allowed where the Secretary of the Interior by his unauthorized and unlawful act and without any semblance of statutory authority had removed the name of an enrolled Indian from the allotment rolls of his tribe and so would have deprived him of his property. It was true his name was removed without notice but the case did not go on that point.

Chicago, Milwaukee etc. Railway Co. v. Board of Railway Commissioners, 76 Mont. 305, is a decision of the Supreme Court of Montana which entirely ignores the principle of the cases above cited that where there is an appeal from the act of a ministerial officer to the Courts as to the *reasonableness* of ministerial action that the due process clause of the Fourteenth Amendment is not challenged.

FAILURE OF DUE PROCESS OF LAW BECAUSE NO STANDARD IS SET UP BY LEGISLATURE

The majority opinion holds:

> "In the instant case the officer is required to exercise legislative power when he sets up a standard and undertakes to say when a business is being conducted in an inequitable manner. Suppose he were directed by the statute to determine when the price of a commodity charged was unreasonable or excessive, or when it was not necessary to provide a reasonable profit, with no direc-

tions or standard to go by; would it not be less complicated than to require him to determine when a business is being conducted in an inequitable manner with no standard in the law as a guide?

"It seems to be generally understood that the main object of the so-called Blue Sky Laws is the prevention of fraud. The police power exercised by the legislature does not go to the extent of regulating or prohibiting the sale of securities or making of contracts based upon the judgment of an investment commissioner or board attempting to insure the public a fair profit on the investment. Nor would the land stand the test if it prohibited such dealing in securities as in the judgment of the commissioner rested upon a plan of organization or conduct of business which was not 'fair.' Ala. & N. O. Trans. Co. vs. Doyle, 210 Fed. 173."

Contrast the language of the opinion with the language in Hall vs. Geiger-Jones, 242 U. S. 551:

"The basis of these contentions is that the law confers arbitrary power upon the commissioner. In considering the contentions we must keep in mind that the law is addressed to a complex situation. Its purpose is, as we have seen, to give a basis for judgment of the securities offered the purchasing public; assure credit where it is deserved and confidence to investment and trading; prevent deception and *save credulity and ignorance from imposition* as far as this can be done by the approved reputation of the seller of the securities and authoritative information.

"It may, however, be said that character establishes itself and neither needs nor can be compelled to accept the stamp of government, and it is asserted that the 'normal investment business of the country' and its 'individual transactions' are not subject to 'executive control,' the broad contention being made that as such business cannot be

prohibited it cannot be regulated. This, indeed, is the basic principle of the opposition to the statute. It is expressed in many ways, and the various provisions of the statute—those that are explicit in direction to the commissioner and those that commit discretion to him—are said to so burden and complicate 'normal business as to make it difficult if not impossible to carry it on in a normal way, if at all.'

"As broadly made, we cannot assent to these propositions. The reason and extent of the law we have indicated and the control to which individual transactions are subjected, and we think both are within the competency of the State. It is to be remembered that the value of securities consists in what they represent, and to determine such value is a complex problem even to the most skillful and informed.

"We have very lately decided a case upon the principle of the power of the State to prevent frauds and impositions. Hutchinson Ice Cream Co. v. Iowa, ante, p. 153. The principle applies as well to securities as to material products, the provisions of the law necessarily varying with the objects. As to material products the purpose may be accomplished by a requirement of inherent purity. The intangibility of securities, they being representatives or purporting to be representatives of something else, of property, it may be, in distant states and countries, schemes of plausible pretensions, requires a difference of provision and the *integrity of the securities can only be assured by the probity of the dealers in them and the information which may be given of them.* This assurance the State has deemed necessary for its welfare to require; and the requirement is not unreasonable or inappropriate. It extends to the general market something of the safeguards that are given to trading upon the exchanges and stock boards of the country, safeguards that experience has adopted as advantageous. In-

convenience may be caused and supervision and surveillance, but this must yield to the public welfare; and against counsel's alarm of consequences, we set the judgment of the state.

"We turn back, therefore, to consider the more specific objections to the law. The basis of them is, as we have seen, the power conferred upon the commissioner, which is asserted to be arbitrary. The objection is somewhat difficult to handle. It centers in the provision that requires the commissioner, as a condition of a license, to 'be satisfied of the good repute in business of such applicant and named agents,' and in the power given him to revoke the license or refuse to renew it upon ascertaining that the licensee 'is of bad business repute; has violated any provision of this act or has engaged, or is about to engage, under favor of such license, in illegitimate business or in fraudulent transactions.' It is especially objected that as to these requirements no standard is given to guide or determine the decision of the commissioner. Therefore, it is contended that the discretion thus vested in the commissioner leaves 'room for the play and action of purely personal and arbitrary power.'

"We are a little surprised that it should be implied that there is anything recondite in a business reputation or its existence as a fact which should require much investigation. If in special cases there may be controversy, those cases the statute takes care of; *an adverse judgment by the commissioner is reviewable by the courts.* Section 6373-8. So also as to the other judgments.

"Besides it is certainly apparent that if the conditions are within the power of the State to impose, they can only be ascertained by an executive officer. Reputation and character are quite tangible attributes, but there can be no legislative definition of them that can automatically attach to or identify individuals possessing them, and necessarily

the aid of some executive agency must be invoked. The contention of appellees would take from government one of its most essential instrumentalities, of which the various national and state commissioners are instances. But the contention may be answered by authority. In Gundling v. Chicago, 177 U. S. 183, an ordinance of the City of Chicago was passed on which required a license of dealers in cigarettes and as a condition of the license that the applicant, if a single individual, all of the members of the firm, if a co-partnership, and any person or persons in charge of the business, if a corporation, should be of good character and reputation, and the duty was delegated to the mayor of the city to determine the existence of the conditions. The ordinance was sustained. To this case may be added Red "C" Oil Manufacturing Co. v. North Carolina, 222 U. S. 380, 394, and cases cited; Mutual Film Corporation v. Industrial Commission of Ohio, 236 U. S. 230; Brazee v. Michigan, 241 U. S. 340, 341. See also Reetz v. Michigan, 188 U. S. 505; Lieberman v. Van De Carr, 199 U. S. 552.

"The discretion of the commissioner is qualified by his duty, and besides, as we have seen, the statute gives judicial review of his action. Pending such review we must accord to the commissioner a proper sense of duty and the presumption that the functions entrusted to him will be executed in the public interest, not wantonly or arbitrarily to deny a license to or take one away from a reputable dealer (Plymouth Coal Co. v. Pennsylvania, 232 U. S. 531, 545); and, as we have said, in cases where there can be a dispute of fact, the statute provides for judicial review, and we see no legal objection to the designation of a particular court for such review."

It is submitted that there is nothing more "recondite" in the proposition as to whether or

not a contract is inequitable than in the proposition as to whether or not a certain concern has a good "business reputation."

The court appears to hold that the due process clause is invaded because the purpose of the statute (to protect against inequitable contracts), is not within the police power of the state although the court does not definitely make this statement in the majority opinion. The opinion states, however:

> "* * * but the Supreme Court held that the purpose of the statute was to protect investors not from financial loss generally but from fraud. Merrick v. N. W. Halsey & Co., 242 U. S. 568."

but we do not so read Merrick v. N. W. Halsey Co.

The court says, speaking of what regulations the state may impose,

> "Besides, it is for the State to judge in such circumstances and the judgment and its execution would have to be palpably arbitrary to justify the interference of the courts."
>
> "It may be that constitutional law must have a more fixed quality than customary law, or, as was said by Mr. Justice Brewer, in Muller v. Oregon, 208 U. S. 412, 420, that 'it is the peculiar value of a written constitution that it places in unchanging form limitations upon legislative action.' This, however, does not mean that the form is so rigid as to make government inadequate to the changing conditions of life, preventing its exertion except by amendments to the organic law. We may feel the difficulties of the new applications which are invoked, the

strength of the contentions and the arguments which support or oppose them, but our surest recourse is in what has been done, and in the pending case we have analogies if not exact examples to guide us. So guided and so informed, we think the statute under review is within the power of the State. It burdens honest business, it is true, but burdens it only that under its forms dishonest business may not be done."

"Engel v. O'Malley, 219 U. S. 128, was not decided because fraud was incidental to the business of banking by individuals or partnerships but because fraud could be practiced in it and that hence it could be licensed. Nor was it decided in Allen v. Riley, 203 U. S. 347, that the transfer of patent rights was of itself illegal or that any particular transfer would be deceptive, but that some transfers might be; and so a statute of Kansas which required any person selling or offering to sell such rights to conform to certain requirements was declared valid. Nor did we hesitate to hold valid the regulation of the business of employment agencies. It was a lawful business and would not in instances be injuriously conducted; but in instances it might be, and because it might be, with injurious consequences, its regulation was provided. This court sustained the regulation and the condition that it was to be enforced according to the legal discretion of a commissioner. Brazee v. Michigan, 241 U. S. 340. See also Brodnax v. Missouri, 219 U. S. 285. Other cases might be cited of similar import."

and see Dillingham vs. McLaughlin, 264 U. S. 370 on page 374.

"Whatever may be one's own opinion about the wisdom of trying to save the ignorant and rash from folly it is a recognized power that is used in many ways."

IT DOES NOT APPEAR ON THE FACE OF THE RECORD THAT THE EVILS DID NOT EXIST IN MONTANA WHICH MAKE THE ENJOINED PROCEDURE AN APPROPRIATE REMEDY

In O'Gorman & Young v. Hartford Insurance Co., 248 U. S. 251:

> "The business of insurance is so far affected with public interest that the State may regulate the rates, and likewise the relations of those engaged in the business.
>
> "A New Jersey statute declaring that rates of insurance against the hazards of fire shall be reasonable, and making it unlawful for a fire insurance company to allow a commission to any person for acting as its local agent respecting such insurance, in excess of that allowed to any of its local agents on such risks in the State, upheld, upon the record in the case as within the power of the State to regulate such rates.
>
> "A state statute, dealing with a subject clearly within the police power, can not be declared void upon the ground that the specific method of regulation prescribed by it is unreasonable in the absence of any factual foundation in the record to overcome the presumption of constitutionality.
>
> "It does not appear upon the face of the record here in question, or from facts of which the Court must take judicial notice, that, in New Jersey, evils do not exist in the business of fire insurance for which the statutory provision is an appropriate remedy. P. 258, 105 N. J. 542, affirmed."

To illustrate: what the commissioner would have done by his proposed order was to fix the limit of forfeiture which an installment invest-

ment company might impose. Certainly such matters as this (what is a reasonable charge for putting the business on the books of the company) have been determined through generations of charges and computations in insurance and like contracts and certainly, as was stated in the Blue Sky cases, if such determination as this cannot be made by the commissioner as the case arises, the legislature is powerless to meet the situation at all.

THE COMPLAINT DOES NOT STATE FACTS SUFFICIENT TO CONSTITUTE A CAUSE OF ACTION AS PLAINTIFF MUST COME IN WITH CLEAN HANDS. HIS CERTIFICATE SET UP IN THE COMPLAINT SHOWS ITS OWN INEQUITY.

> "The complainant is first adjudged and not until he has been found free from taint does equity proceed to determine whether or not he has been wronged."—Fay vs. Lambourne, 214 App. Div. 245, 247; 108 N. Y. S. 864, (Affirmed 186 N. Y. 575. mem. 90 N. E. 1158 mem.)
>
> "Nothing can call a court of chancery into activity but conscience, good faith, and reasonable diligence; and where these are wanting, the court is passive and does nothing."—McKnight v. Taylor, 1 How. (U. S.) 161, 168, 11 L. Ed. 86.

Let us examine plaintiff's hands in this action:

> "The Investors Syndicate has approximately ten million in contracts in effect in Montana and for the year 1930 the cash receipts from the state were $309,456.02, represented in 4437 certificates in force at the end of the year. There were 802 certificate

lapsations during the year, representing 18% of the certificates in force and 15% of the total face amount in force."

The following are computations of losses which follow from forfeiture of plaintiff's contract as set out in the exhibit attached to Bill of Complaint, R. p. 10a to 10e:

"a. The loss in equity to be suffered by any investor who found himself unable to continue the installment payments and accepted a cash settlement upon surrender of such certificate prior to maturity, i. e.

1. The loss as measured by the difference between the cash payments plus the accrued interest thereon and the cash to be paid the investor upon surrender of the certificate, the percentage of equity loss being:

x. Under the annual payment plan:

73.1%	at	end	of	18	months
47.6%	"	"	"	2	years
32.9%	"	"	"	3	"
25.1%	"	"	"	4	"
15.1%	"	"	"	5	"
13.0%	"	"	"	6	"
10.1%	"	"	"	7	"
7.2%	"	"	"	8	"
5.5%	"	"	"	9	"

The table is figured on the basis of a $1,000.00 certificate.

LOSS IN EQUITY

Annual Basis ($74.00 *each year in advance*)

Year	Cumulative Cash Payments	Interest 5½ % Comp. Annually	Amount at End of Year	Cash Surrender Values	Loss in Amount:	Equity Percent
1st	$ 74.00	$ 4.07	$ 78.97	$ 42.00	$114.25*	$73.1*
2nd	148.00	8.36	160.43	84.00	76.43	47.6
3rd	222.00	12.89	247.32	166.00	81.32	32.9
4th	296.00	17.67	338.99	254.00	84.99	25.1
5th	370.00	22.71	435.70	370.00	65.70	15.1
6th	444.00	28.03	537.73	468.00	69.73	13.0
7th	518.00	33.65	645.39	580.00	65.38	10.1
8th	592.00	39.57	758.95	704.00	54.95	7.2
9th	666.00	45.81	878.76	830.00	48.76	5.5

*The first cash surrender value allowed is at the end of eighteen months, during which time the accumulated amount is:

On the annual basis $156.25
On the monthly basis 122.15

The business scheme pays about the same rate of interest as is paid on a good standard form of bond investment—5½%—and certainly in a business promising to return that moderate amount of money which causes an unfortunate to lose 73% of the amount that he has paid in at the end of a year if unable to continue with his installments does not highly recommend the promoter of such a scheme in a court of equity.

Note the evidence placed before the commissioner on the hearing as to the order:

> "Mr. P. C. Bulen, President of the Montana States Building and Loan Association, Great Falls, Montana, testified and introduced as an exhibit a contract entered into between C. Everett or Carrie Davis and an investment company, for $10,000.00 installment thrift bond contract. He stated that at the end of 36 months the subscribers had paid in $1260.00 and that the withdrawal value at the end of three years was $625.00, leaving a loading charge, exclusive of accrued dividends and interest, of $624.00. In other words, at the end of 36 months the loss to the subscribers was $624.00."

It is submitted that a complaint showing such an extortionate scheme hidden in a wilderness of print does not commend itself to equity.

CONCLUSION

The decree of the lower court granting an injunction should be reversed and the case remanded with directions to dismiss.

Respectfully submitted,

L. A. FOOT,

Attorney General of the

State of Montana,

T. H. MacDONALD,

Assistant Attorney General

of the State of Montana,

Attorneys for Appellant.

Service of the above and foregoing Appellant's Brief admitted and receipt of a copy thereof acknowledged this.....day of April, 1932.

.....

.....

Attorneys for Appellee.

FILE COPY

No. 627

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GEORGE P. PORTER, State Auditor and ex officio Investment Commissioner of the State of Montana, Appellant

vs.

INVESTORS SYNDICATE, a corporation, Appellee.

BRIEF ON REHEARING

L. A. FOOT,
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ASSISTANT ATTORNEY GENERAL

ATTORNEYS FOR APPELLANT.

MAGGLE PRINTING CO., HELENA, MONT.

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BRIEF ON REHEARING

The sole ground of the motion for rehearing in this case is set forth on page two of the Petition for Rehearing as follows:

> "Section 29 of Article III of the Montana Constitution provides:
>
> > 'The provisions of this Constitution are mandatory and prohibitory, unless by express words they are declared to be otherwise."

> "As this Court has decided that the power sought to be conferred upon the Court by Section 4038 as amended is not judicial but administrative, said section is clearly violative of Section 1 of Article IV of the Montana Constitution."

Petitioner cites In re Weston, 28 Mont., 207, 219. This was a case where the legislature attempted to make it imperative on the Supreme Court to disqualify certain judges of the state on the presentation of an affidavit and it was held:

> "Under Constitution, Article IV, Section 1, the legislature cannot impose upon the supreme court, or its justices, the performance of an act not judicial in its character but *purely* ministerial or executive."

The distinction between the Weston case and this case is that the function to be performed by the courts of Montana in case of an appeal thereto from the decision of the Commissioner is not *purely* legislative or ministerial.

The question involved in the petition for rehearing is: Will the Courts of Montana assume jurisdiction of a case where they must perform legislative as well as judicial functions. The principle has been decided by the Montana Supreme Court in O'Neil vs. Yellowstone Irrigation District, 44 Mont. 506-507.

> "It is undoubtedly true that no case can be found in which a statute imposing purely legis-

lative functions upon courts has been upheld; but, as shown by the cases cited, where the principal power conferred is judicial in character, the fact that the exercise of the power so conferred may incidentally require *the exercise also of legislative or administrative functions* does not impair the validity of the legislation conferring it. The duty to determine the propriety of establishing irrigation districts, resting, as it does, upon public necessity, appertains exclusively to the law-making body. So, also, the mode by which they may be organized must be determined by it. But the ascertainment of the necessity or utility of establishing a particular district, as well as the solution of the question whether the conditions precedent have been complied with, involve judicial functions, the exercise of which is properly left to the courts. It is sufficient to sustain the law if the general power conferred is judicial, though it incidentally requires the performance of legislative and administrative duties. (State vs. Barker, 116 Iowa, 96, 93 Am. Rep. 222, 89 N. W. 204, 57 L. R. A. 244; Sanderlin v. Luken, supra; State ex rel. Matson v. Superior Court, supra)".

Does the appellee and petitioner have the right to a preliminary injunction on appeal to the Courts of Montana.

This question has likewise been decided by the Supreme Court of Montana in State vs. District Court, 53 Mont. 229.

"Has the district court in this class of cases jurisdiction to use the provisional remedy of injunction *in limine* to suspend an order or regulation made and promulgated by the board pending a final determination of the action in which a review of the order is sought."

This case reviewed the action of the railroad commission in establishing certain rates for railroads.

"The board is vested with very extensive powers and duties. Among numerous others it has power, and it is its duty, to establish and promulgate fair and just rates and charges for the transportation of passengers and freight by railroads operating in this state; to prevent extortion and unjust discrimination in this behalf, and to compel all such railroads to provide and maintain train service for both passengers and freight, * * *"

"Section 4384 confers upon the district court of the proper county jurisdiction to review any determination of the board 'fixing any classification, rate, toll, charge, regulation, or order,' or its refusal to make, fix or establish such classification, rate, etc. The action must be commenced by the filing of a complaint in the proper county, and the defendant must be served with summons as in an ordinary action, or with an order of court fixing a reasonable time within which appearance may be made, not less than five days. The issues are made up by answer. If the court finds the order classification, rate, toll, charge, regulation, or

establishing the classification, rate, etc., to be unjust and unreasonable, *it becomes the duty of the board to revise it.* Section 4390 authorizes any railroad deeming a classification, rate, toll, etc., established by the board to have its determination reviewed."

"Section 4390 contains two provisos, viz: 'That until the final decision in any such action the order of the board affecting rates or charges shall be deemed to be final and conclusive: And provided, further, that in any action, hearing or proceeding in any court, the classification, rate, tolls, charges, regulations and orders made, fixed and established by said board shall *prima facie* be deemed to be just, reasonable and proper."

"Though the determinations of the board are *prima facie* just and reasonable, this furnishes no compelling reason why the presumption in their favor *may not be so satisfactorily overcome by evidence on the hearing of the application that the court would be constrained to grant relief,* just as it would in any other case. Inasmuch as the jurisdiction conferred is general, except so far as the legislature has expressly restricted it, we do not think that this court should impose any other restriction. It may be that the legislature should have imposed the same restriction as to all orders. This was for that body to determine, and not for the court. Doubtless it deemed it better to leave the whole matter to the exercise of a wise judicial discretion, anticipating that cases might

arise in which the order complained of would be so clearly oppressive that immediate relief from it would be imperative. It may be assumed that, since the legislature has expressly declared that all the determinations of the board are to be deemed prima facie just and reasonable, the court should exercise its discretion with reserve and caution. This consideration, however, is one affecting the mode of exercising the jurisdiction conferred, and is not pertinent to the inquiry whether the legislature intended to confer it."

The language of the statute in question in this case is Section 4038, as amended by Chapter 194 of the Session Laws of 1931. So far as it pertains to the matter of preliminary injunction is:

> "Pending any such action, the said findings or decision of said commissioner shall be prima facie evidence that they are just and reasonable and that the facts found are true, and pending any such action the said findings or decision of the commissioner shall remain in full force and effect. If no action be brought to set aside said findings or decision within thirty days, the same shall become final and binding."

The concluding words of the paragraph "If no action has been brought to set aside said findings or decision within thirty days, the same shall become final and binding" clearly convey the impression that the findings and decision of the commissioner shall not become final and binding for

thirty days, and then only in the event that the action has not been brought. The effect of the words "pending any such action said findings and decision shall be prima facie evidence", have no force as against a preliminary injunction as was decided in the case of State vs. District Court, above quoted from.

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ATTORNEYS FOR APPELLANT.